

Final Decision

Review of the Requirements for Railway Owners to Submit
Floor and Ceiling Costs

August 2011

Economic Regulation Authority



WESTERN AUSTRALIA

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Overview

1. The Economic Regulation Authority (Authority) administers the *Railways (Access) Act 1998* (Act) and the *Railways (Access) Code 2000* (Code). The Code is a requirement of the Act and both became effective in 2001.
2. The Authority's role is to oversee, monitor and enforce compliance with the Act and the Code, together referred to as the WA Rail Access Regime (Regime). The rail network and types of infrastructure subject to the Regime are defined in Schedule 1 of the Code.
3. The Authority is currently reviewing the requirements for WestNet Rail (WNR) and The Pilbara Infrastructure (TPI) to submit floor and ceiling costs for review by the Authority.
4. The Authority has previously reviewed the requirements for the Public Transport Authority (PTA) to submit floor and ceiling costs. In 2009, following public consultation, the Authority decided that it would not undertake future reviews of PTA's floor and ceiling costs, except where required under clause 9 or clause 10, Schedule 4 of the Code in response to an actual or expected proposal by an access seeker.
5. Documents relating to that review may be found on the Authority's website, at: [http://www.erawa.com.au/3/1114/48/compliance_arrangements_public_transport_a
uthorit.pm](http://www.erawa.com.au/3/1114/48/compliance_arrangements_public_transport_authorit.pm)
6. The Authority published an Issues Paper in May 2011 outlining some matters for consideration in the current review. In the issues paper, the Authority stated that it would make a final decision on the requirements for railway owners to submit floor and ceiling costs following receipt of submissions from stakeholders in response to the issues paper.
7. Following consideration of issues raised in submissions, the Authority has decided to adopt the following processes in administering the requirements of the Code:
 - The Authority will require railway owners to submit floor and ceiling costs for their network on commencement of the application of the WA Rail Access Regime to their network.

This mirrors current Authority practice.
 - Consultation under clause 9 (Schedule 4) for determinations in respect of route sections for which costs are being determined for the first time will incorporate the publication of the railway owner's initial determination and the Authority's final determination on the Authority's website.

This mirrors current Authority practice.
 - If an access proposal is received, the railway owner must notify the Authority and must submit an initial determination of costs as required under clause 10 (Schedule 4) of the Code.

This is a requirement of the Code, and indicates the means by which a determination is initiated if an access proposal is received by a railway owner.

- Costs for route sections previously determined under clause 9 or 10 may be redetermined by the Authority under clause 9 if the Authority expects it likely that a new access proposal will be made.

This mirrors current Authority practice.

- All floor and ceiling costs which are published in relation to clause 9 or 10 determinations which proceed to an agreement under the Code will apply for five years and will incorporate four subsequent annual adjustments by the railway owner to adjust ceiling costs for changes in CPI and the WACC published annually by the Authority.

Current Authority practice is for determinations to apply for three years, and to incorporate two annual adjustments.

- At the expiration of the five year period, the Authority will not require the railway owner to submit costs for redetermination.

This is a modification of current Authority practice, which requires an automatic re-determination on the expiration of the previous determination.

- Costs for route sections previously subject to a determination under clause 9 or 10 may be redetermined by the Authority under clause 12 (Schedule 4) in response to a request in writing from the railway owner.

Clause 12 is the mechanism that will be used by the Authority to enable a railway owner to initiate a redetermination of costs, if a railway owner wishes costs on a route or route section to be redetermined.

8. The term “initial determination” reflects the wording used in Schedule 4 of the Code to describe the proposed floor and ceiling costs required to be submitted by railway owners in accordance with clauses 9 and 10. The Code draws a distinction between the initial determination of costs by railway owners and the determinations made by the Regulator.
9. These decisions reflect amendments to administrative arrangements which do not require amendments to the Code.
10. Further changes to compliance arrangements for railway owners, such as review periods for Part 5 instruments, are being addressed in the Authority’s current review of the Code. The changes contemplated in that review would require amendment to legislation.

The WA Railway Access Regime and legislative obligations on railway owners

11. The railway networks covered by the Regime are set out in Schedule 1 of the Code and includes 5,000 route kilometres of rail track operated by WNR, the urban

passenger network operated by the PTA, and the railway owned by TPI into Port Hedland.

Segregation Arrangements and Part 5 instruments

12. Section 28 of the Act requires that railway owners must prepare a Segregation Arrangements document, which outlines how a railway owner will 'ring-fence' its below-rail and above-rail operations (where the railway owner operates its own rolling stock on the railway) such that third parties seeking access to the rail network are not unfairly disadvantaged compared with the railway owner's own above-rail operation. The Segregation Arrangements must provide for the key elements of protection of confidential information, avoidance of conflict of interest, duty of fairness, and maintenance of separate accounts and records.
13. In addition to the requirement to segregate as outlined in Section 28 of the Act, Part 5 of the Code details requirements to prepare four regulatory instruments, referred to collectively as 'Part 5 instruments'. The four Part 5 instruments are the Train Management Guidelines, the Train Path Policy, the Costing Principles and the Over-payment Rules. Railway owners must prepare documents demonstrating their compliance with the requirements of the Code and submit these to the Authority for approval.
14. The Code does not require the Regulator to publish railway owners' Part 5 instruments. The practice of the Authority has been to publish these instruments in order to disseminate information which would assist persons who may become involved in negotiations with railway owners under Part 3 of the Code.

Floor and Ceiling Cost Determinations

15. Pursuant to the requirements of the Code, a railway owner must prepare an initial determination of ceiling (maximum) and floor (minimum) costs applicable to those sections of its network on which the Regulator considers it likely that an access proposal is likely to be made, or if an access proposal is actually made. An access proposal is defined in section 8, Part 2 of the Code.
16. If the Regulator considers it likely that an access proposal will be made, then a determination of costs is required under clause 9. If an access proposal is actually made, then a determination is required under clause 10.
17. The Authority must review the railway owner's initial determination and make its own determination on the floor and ceiling costs to apply to the route sections subject to the likely or actual access proposal.
18. The Authority is required to consult with stakeholders in relation to floor and ceiling cost determinations only where the determination is required under clause 9. The Authority is not required to consult with stakeholders in relation to clause 10 floor and ceiling cost determinations. Clause 11 (Schedule 4) relates to floor and ceiling determinations made under clause 10 and states that:

The regulator may, in such manner as he or she thinks fit –

 - (a) *Give public notification of the matters he or she is called upon to approve under clause 10(3); and*
 - (b) *Give persons an opportunity to make submissions on them.*
19. The Code does not require the Regulator to:
 - (a) make public the railway owner's initial determination, or

- (b) publish the Authority's final determination as part of the consultation process required under clause 9.
20. Clause 12 of the Code applies if the Regulator considers that there has been, or may have been, a material change in circumstances that existed at the time when he or she approved or determined costs under clause 9 or 10. In these instances the Regulator provides a determination of costs, and may provide public notification and give persons an opportunity to make submissions on the determination. Clause 12 does not require that the railway owner submit an initial determination as part of this process.

Provision of Information

21. Section 48 of Part 6 of the Code requires that any information given to a proponent by a railway owner in response to an access proposal (i.e. the information outlined in section 9(1)(c)) must be provided to any other entity who requests it.
22. Section 50 of Part 6 of the Code outlines that it is a function of the Regulator to disseminate information that relates to the carrying out of matters provided for by the Regime, including information which would assist persons who are involved in negotiations under Part 3 or who may become so involved.

Current arrangements for submission of floor and ceiling cost proposals by railway owners

23. WNR first submitted floor and ceiling costs in January 2003, for 23 route sections. The determination of floor and ceiling costs by the Regulator was made under clause 9 of the Code in that first instance, in view of the application of the Act and the Code to the WNR network for the first time.
24. Each subsequent determination on floor and ceiling costs by the Authority has required that WNR resubmit floor and ceiling costs for these and any other nominated route sections at regular three yearly intervals. Each determination published by the Authority has applied for three years and incorporates a determination for the initial year and provision for adjustments in the subsequent two years.
25. A requirement for periodic review of floor and ceiling costs is not set out in the legislation, but has been stipulated in each floor and ceiling cost determination published by the Authority. As an example, paragraph 234 of the Authority's final determination on WNR floor and ceiling costs (30 June 2009) states:
- The floor and ceiling costs indicated in this Final Determination will apply from 1 July 2009 to 30 June 2012 with annual adjustments as set out in WNR's Costing Principles. WNR will be required to submit its proposed revisions to its floor and ceiling costs nine months prior (1 October 2011) to the date from which the next determination on its floor and ceiling costs will apply (1 July 2012).*
26. TPI submitted its first floor and ceiling cost initial determination in July 2010 for its Cloudbreak to Port Hedland route section. The Authority has suspended its review of these costs on the basis that the TPI network has been subsequently expanded, and that the costs associated with operating the Cloudbreak-Port Hedland route section must therefore be re-assessed.

Public Consultation

27. On 11 May 2011, the Authority issued a notice calling for submissions from interested parties on the matters outlined in an Issues Paper “Review of the Requirements for Railway Owners to Submit Floor and Ceiling Cost Proposals”. The closing date for submissions was 10 June 2011.
28. Eight submission were received, from:
 - Alcoa World Alumina Australia (Alcoa)
 - Association of Mining and Exploration Companies (AMEC)
 - Asciano (ASCIANO)
 - CBH Operations, Co-operative Bulk Handling (CBH)
 - Geraldton Iron Ore Alliance (GIOA)
 - North West Infrastructure (NWI)
 - Oakajee Port and Rail (OPR)
 - WestNet Rail (WNR)
29. Some comments made in the public submissions are outside the scope of matters considered by the Authority in relation to this review. For example, comments submitted which relate to the appropriateness of the Modern Equivalent Asset (valuation) conventions are not addressed in this decision document.
30. The Authority is currently progressing a review of the Code, and a final report from that review will be presented to the Treasurer. The Authority will consider some of the issues raised in this consultation in conjunction with that review.
31. A number of comments in public submissions referred to the usefulness of floor and ceiling cost determinations in assisting negotiations outside the Code. The Authority acknowledges that whilst information published on the Authority’s website can be referred to for any purpose, Code instruments are not published in order to assist negotiations made outside of the Code. The Authority considers that retaining the current arrangements which impose regulatory costs in order to assist out-of-Code negotiations would be inconsistent with the light-handed negotiate-arbitrate nature of the WA Railway Access Regime.
32. A number of comments in public submissions referred to “Floor and Ceiling Prices”, and specifically to requirements for railway owners to provide access prices for review and for the Regulator to publish access prices. The Authority notes that the Code does not require that railway owners provide access prices for review, or that the Regulator make determinations on floor and ceiling prices.
33. The Authority notes that the terms ‘floor price’ and ‘ceiling price’ appear in the Code only in the titles of clauses 7 and 8 (Schedule 4), and in section 9 (Part 2) of the Code. Clauses 7 and 8 are clauses relating to the administration of the railway owner’s Over-payment rules, and section 9 relates to the information a railway owner must provide on receipt of an access proposal.
34. The use of the terms ‘floor price’ and ‘ceiling price’ in these contexts relates only to the minimum and maximum amounts recoverable by the railway owner in respect of a route, or payable by the operator if they are the only operator on the route.

Discussion of matters raised in the Issues Paper

35. Comments made in public submissions which relate to the matters listed in paragraph 37 of the Issues Paper, under the heading “Issues”, are addressed below.

ISSUE 1: Do regular floor and ceiling cost reviews potentially require duplication of effort on the part of the Railway Owner if an access proposal is received for a set of route sections for which floor and ceiling costs have not been determined?

Issue 1 relates to a situation where an access proposal is received on a subsection of a route. If costs have been determined at the route level, but not at the subsection level, a cost determination for the subsection is required to be made. This might be considered a duplication of effort, especially if an access proposal for the route in its entirety is unlikely to be received.

Comments in Submissions

36. GIOA made the assertion in its submission that:
- if an access proposal is made a cost determination is required regardless of whether a line section has pre-determined costs published on the Authority's web site.*
37. OPR submitted that requiring railway owners to submit floor and ceiling costs in the absence of an access proposal is a duplication of effort that places unnecessary compliance costs on railway owners.
38. GIOA submitted that, if access is negotiated outside the Code, published costs are required as a negotiation guide.
39. WNR submitted that there is substantial potential for duplicated effort for both the Regulator and the railway owner where cost determinations are required in the absence of an access proposal. WNR argued that it is not the case that costs previously approved would be automatically applicable or accepted by the Regulator, in which case duplication of work would be required.

Authority Response to Comments

40. While the Authority acknowledges that an initial determination is required to be submitted by the railway owner in the event that an access proposal has been made, i.e. requiring a clause 10 determination, it is not clear that this necessarily requires a duplication of effort. The Authority takes the position that if a determination is published on the Authority's website, and the railway owner wishes that determination to apply to a new access proposal, then the railway owner may submit an initial determination which coincides with the determination published on the Authority's website for the relevant route section, and it is appropriate for that determination to be considered for approval on that basis. This mirrors the current practice of the Authority.
41. The Authority agrees with the GIOA assertion that if an access proposal is made a cost determination is required regardless of whether a line section has pre-determined costs published on the Authority's website. The Authority does not

agree with the OPR assertion that requiring regular floor and ceiling cost determinations necessarily requires a duplication of effort.

42. It is important to note that the cost determination for a route section does not determine the price that an access seeker is charged for access to that route section. The cost determination is used in determining maximum cost recovery for the purposes of the ceiling price test described in clause 8 of the Code, and is used to monitor the Over-payment Rules as they apply to that route section.
43. If an access agreement is current under the Code, then a determination of costs is required to be used for the purposes of administering the railway owner's Over-payment account.
44. Moreover, a cost determination does not necessarily remain current for the duration of the contract made between the railway owner and the access seeker, and the cost determination may subsequently be updated by the railway owner. The ceiling cost for that route section may increase over time regardless of the terms of the contract between the railway owner and an individual operator. This may be the case where a subsequent access agreement is made with an additional operator on the same route section, especially if the subsequent access agreement requires a route expansion or extension.
45. With reference to comments by GIOA, in relation to the usefulness of published cost determinations in assisting negotiations outside the Code, the Authority notes that Code instruments are not intended to support negotiations made outside the Code. The Authority considers that publishing railway owners' information in order to assist out-of-Code negotiations would be inconsistent with the light-handed negotiate-arbitrate nature of the WA Railway Access Regime.

Authority View: Issue 1

46. The Authority considers that following the determination of costs for a route, a redetermination of costs for the same route is an unnecessary regulatory requirement in the absence of an access proposal being made for all or part of that route.
47. This is because the current practice of the Authority, which is reflected in railway owners' costing principles, is to require the railway owner to provide a costing model which contains sufficient technical information required to calculate the replacement cost for the route as part of a railway owner's initial determination.

ISSUE 2: Would regular reviews of floor and ceiling costs assist the railway owner in the event of a proposal being made, by ensuring that route section costs are instantly available?

Regardless of whether a cost determination for a route or a route section is published on the Authority's website and is considered 'current', a railway owner must provide an initial determination of costs in every instance that a determination is required under clauses 9 or 10. In the event that a determination is required in response to an actual or likely access proposal which does not require capital expansion on the route, then the railway owner might choose to submit a determination which coincides with the

determination which is current on the Authority's website and it may be considered by the Authority for approval on that basis.

Comments in Submissions

48. GIOA submitted its view that regular reviews of floor and ceiling costs assist the railway owner in the event of a proposal being made, by ensuring that route section costs are instantly available.
49. ASCIANO submitted that continuation of the existing regulatory process may benefit both WNR and the ERA, as it enables the regulatory process to be continued at an incremental cost.
50. NWI submitted that:

The pricing mechanism for rail infrastructure should be done on an individual "Section of Line" basis as this is the most efficient method of recovering the cost of providing individual elements of rail infrastructure.
51. WNR submitted that mandated regular cost reviews do not provide a readiness that would be otherwise unavailable to the railway owner. WNR argued that it is prudent for the railway owner to maintain an ability to calculate up-to-date costs for any part of the network as a normal business practice. WNR argued that for this reason, and as the Regulator may redetermine costs under clause 12 at any time, regular reviews do not improve the ability of a railway owner to respond to access requests, and that the absence of regular reviews would not diminish that ability.

Authority Response to Comments

52. In relation to GIOA's view that regular reviews of floor and ceiling costs assist the railway owner in the event of a proposal being made, by ensuring that route section costs are instantly available, the Authority notes that this would be true where the railway owner wishes to use a previous determination as the basis for a new access proposal. The Authority notes that where capital expansions are required to meet the requirements of an access proposal, the railway owner may find it necessary to provide a revised cost determination.
53. With reference to ASCIANO's view that regular publishing of floor and ceiling cost determinations enables the continuation of the regulatory process at incremental cost, the Authority must consider this assertion in the context of the question of whether or not a continuation of the current processes remains appropriate. In terms of cost effectiveness alone, a balance between the potential cost imposts associated with duplication and cost savings associated with minimising incremental cost is not established in ASCIANO's argument.
54. In relation to the NWI submission that a pricing mechanism should be defined on a section of line basis, the Authority notes that there is no 'floor and ceiling pricing' mechanism defined in the Code. The Code only requires that costs be submitted by railway owners, under certain circumstances. The Authority also notes that there is no requirement in the Code for costing information to be determined on any other basis than on the basis of the actual route section(s) for which access is (or is considered likely to be) sought.
55. In relation to the WNR submission, the Authority notes that considerable effort has been made by WNR to provide a costing model for publication on the Authority website which is comprehensive and up to date. WNR has provided this model to

ensure a high level of transparency in costs and to enable timely verification of cost adjustments published by the Authority from time to time.

56. There is no requirement for the Authority to publish floor and ceiling cost determinations on its website, or to publish initial determinations from railway owners as part of any consultation process.

Authority View: Issue 2

57. The Authority does not consider that regular reviews of floor and ceiling costs assist the railway owner in the event of an access proposal being made, by ensuring route section replacement costs are readily available. The Authority considers that prudent business practices, in addition to the Authority's requirements to prepare costing models, would ensure that railway owners are well placed to meet the time requirements outlined in the Code for the provision of cost determinations.
58. The Authority notes that section 9 of the Code, which relates to a railway owner's obligations on receipt of an access proposal, requires that the railway owner must within 7 days after a proposal is received provide the proponent with the floor and ceiling costs attributable to the routes subject to the proposal.
59. Accordingly, there is a statutory requirement that railway owners maintain a capacity to calculate route replacement costs on short notice.

ISSUE 3: Is there an advantage to the access seeker in having determined floor and ceiling costs available on the Authority's website, as opposed to discovering those via the proposal process?

Costs which are determined for routes or route sections and published on the Authority's website are published as a means of meeting the requirements of sections 48 and 50 of the Code. These sections, together, require that any information provided to a proponent by a railway owner in response to an access proposal must be provided to any other entity which requests it, and that the Regulator must disseminate any information which would assist persons who are involved in negotiations under Part 3 or who may become so involved.

Published cost determinations do not apply to new access proposals, and are published only to provide an indication of costs previously determined. A new initial cost determination must be submitted by the railway owner in the event of a clause 9 or 10 determination being required.

In the event that an access proposal is received which does not require any capital expansion to any part of the route, then the railway owner may choose to submit an initial cost determination which coincides with an existing determination.

The issue here is the usefulness of a previous determination in informing a new access proposal, and the degree to which any changes in a railway owner's initial determination may compromise that usefulness.

Comments in Submissions

60. GIOA submitted that:

the availability of route section costs are essential to developing and expanding bulk commodity export projects, and are critical to the assessment of development options, staging and financial feasibility. Estimation of capital charges and access charges are required to model mining and above rail feasibility without the need to seek such information under an access application.

61. AMEC submitted:

it is an essential requirement for clarity and certainty in the decision making processes, that railway owners continue to make publicly available 'floor and ceiling cost proposals'. Such an approach will also ensure that competition on relevant rail networks is transparent and fair.

62. ASCIANO submitted:

Ongoing provision of a consistent series of maximum and minimum costs will generally provide a sufficient level of information to access seekers

There is a substantial benefit to the access seeker in having pre-determined maximum and minimum costs available, as opposed to discovering these via the access proposal process. The availability of such pre-determined costs will allow any access seeker to approach a railway owner with an access proposal.

Any decision to cease providing maximum and minimum costs may be premature and may actually result in increased costs when proposals for access are submitted.

63. NWI submitted that the absence of published floor and ceiling prices makes it more difficult for an access seeker to prepare an informed proposal, and

In the scenario which includes capacity additions, or a restructure of sections of line, the Provisional Information would include the extra capacity cost for which there would be no reference to price to compare with the proposed price (including capacity increase), and therefore it would be impossible to calculate the cost of the extra capacity and assess if this was reasonable.

64. OPR submitted that there do not appear to be any significant costs accruing to access seekers by the ERA changing the current arrangements.

65. WNR submitted that there is no advantage to an access seeker in having floor and ceiling costs available on the Authority's website. WNR considers it likely that any access request under the Regime would contemplate sections of the network which are already utilised by one or more operators, and that an individual operator's access price can be substantially affected by the price paid by other operators (inside and outside the Regime). Given the confidential nature of commercial access arrangements, the railway owner is not obliged to provide information on the amounts paid by other operators. WNR submitted that, this being the case, publicly available up-to-date floor and ceiling costs do not offer access seekers information that would enable them to make anything but the broadest of price-based commercial decisions.

Authority Response to Comments

66. In relation to GIOA's and AMEC's view, the Authority agrees that a basic level of ongoing cost transparency, although not required under the Code, is advantageous to the achievement of the objectives of the rail regime.

67. In relation to ASCIANO's view, the Authority notes that costs are not required to be determined prior to an access proposal being lodged. The ASCIANO submission does not detail the manner in which the absence of floor and ceiling costs would result in increased costs when access proposals are submitted. The Authority notes that price negotiations commence following the access proposal being made by the access seeker.
68. In relation to the NWI assertion that "the absence of floor and ceiling prices makes it more difficult for an access seeker to prepare an Informed Proposal", the Authority notes that an access proposal, as defined in section 8 (Part 2) of the Code does not include price elements, and that the railway owner initiates negotiation on prices following the lodgement of an access proposal. The Authority again notes that 'floor and ceiling prices' are not defined in the Code.
69. In relation to the NWI reference to 'Provisional Information' in its submission, the Authority takes this to mean Preliminary Information as defined in section 7 (Part 2) of the Code. The Authority notes that pre-determined costs for a route section may provide some assistance in assessing the incremental cost of providing capacity expansion to that route section, but that capacity expansion costs would be assessed by access seekers, using in-house or consulting engineers, as a normal part of any negotiation for access to infrastructure.
70. In relation to the WNR submission, the Authority agrees that the intent of the Code is to provide transparency in costs, not transparency in prices.

Authority View: Issue 3

71. The Authority can envisage only limited circumstances under which a railway owner would choose to submit an initial determination which coincides with an earlier determination for the purposes of meeting the requirements of section 10 (or 9) of the Code. Those circumstances would include if no capital expansions or augmentations were required to meet the needs of the operator making the new access proposal. The only circumstances when a predetermined cost might be useful in indicating an access price would be if no capital expansions or augmentations were required, and there were no other entities, operating under agreements made inside or outside the Code, with access to that route.
72. On that basis, the Authority sees only limited circumstances when an existing determination would provide any more than a broad usefulness in indicating the likely terms to be offered by a railway owner in the event of an access proposal being made.
73. By far, the most useful component of existing determinations is the railway owner's costing model, which the Authority currently publishes as a part of every determination. The costing model provides sufficient technical information for potential access seekers to estimate route replacement costs and route expansion costs which may apply to any future access proposal. The Authority will continue to publish railway owners' costing models.

ISSUE 4: Would the availability of “pre-determined” floor and ceiling costs on the Authority’s website minimise the likelihood that a potential access seeker will seek to have the Authority instigate a floor and ceiling cost determination for a combination of route sections (under Clause 9) but rather approach the Railway Owner directly with a proposal, thereby initiating a determination under Clause 10?

There are two circumstances envisaged in the Code where a railway owner is required to submit an initial determination of costs for a route. Those are when the Regulator considers it likely that an access proposal will be made (clause 9), and under clause 10 if an access proposal is actually made.

There has never been an access proposal put to a railway owner under the WA Railways Access Regime and the initial determinations required to be made by railway owners have to date been a result of clause 9 determinations initiated by the Regulator. The Authority has published its determinations in these instances by way of meeting its responsibility under section 50 (Part 6) of the Code requiring the Regulator to disseminate information that would assist persons who are involved in negotiations under Part 3 or who may become so involved.

The Authority has, from time to time, been approached by potential access seekers who have sought to have costs determined for sections of a railway owner’s network, but who have not proceeded to negotiate for access with the railway owner under the Code.

The Authority is mindful that determinations required under clause 9, require that the Regulator provide an opportunity for public consultation on the determination. Determinations under clause 9 therefore have the potential to result in the disclosure of commercial information belonging to both the access seeker (in terms of their downstream markets for example) and the railway owner (in terms of some aspects of their operating cost structure), which may not be appropriate to disclose if an access agreement under the Code does not proceed.

Comments in Submissions

74. WNR submitted that this issue is of no matter, as the same amount of work is required regardless of whether a cost determination is required under clause 9 or clause 10.

Authority Response to Comments

75. The Authority notes that public consultation requirements are different under clauses 9 and 10. A determination instigated under clause 9 has the potential to result in public disclosure of information which may be relevant only to a specific access proposal. Such information may be commercially sensitive, especially in the case of mining-related proposals.

Authority View: Issue 4

76. The Authority has not received any advice to indicate that the continued availability of determined costs on the Authority’s website will serve to encourage access seekers to approach the railway owner directly with a proposal rather than seek to have the Authority initiate a cost determination under clause 9.

ISSUE 5: In the absence of pre-determined route section costs, do the provisions of Clauses 9 and 10 of Schedule 4 of the Code allow sufficient time for an adequate review of proposed floor and ceiling costs to be undertaken?

Consideration of this issue is intended, without prejudging any advice on the suitability of Code timeframes that the Authority may make in its final report on the review of *the Railways (Access) Code 2000*, to explore whether or not the existence of determined costs on the Authority's website makes any difference to a railway owner's ability to meet the time requirements outlined in the Code.

Comments in Submissions

77. GIOA submitted that in the absence of determined costs, the railway owner will be unable to meet the timelines in the Code, and that the provisions of the Code may not always allow sufficient time for maximum and minimum costs to be adequately prepared and reviewed.
78. NWI submitted that a regular review process would assist the railway owner to keep their route section costs accurate, and would ensure that railway owners were able to meet the access response times required under the Code and the Costing Principles.

Authority Response to Comments

79. The Authority notes that clause 9 does not provide timelines and the process is open-ended. Clause 10 provides for a timeline of 30 days, with provision for extensions as required with the agreement of the access seeker. The Authority also notes that public consultation is not required by the Code in the event of a cost determination under clause 10.

Authority View: Issue 5

80. The Authority can envision only limited circumstances under which a railway owner would choose to submit an initial determination which coincides with an earlier determination for the purposes of meeting the requirements of section 10 (or 9) of the Code. It is only in such circumstances that the existence of a cost determination on the Authority's website may make a material difference to the achievement of timelines for information provision by the railway owner.

Additional Matters raised in Public Submissions

81. This section summarises views put in submissions which do not relate directly to the five issues nominated by the Authority in the Issues Paper. A description of each view is followed by an Authority view on that matter.
82. A number of submissions put the view that published floor and ceiling costs are necessary or are useful in assisting agreements between railway owners and operators negotiated outside the Code. This view was put by GIOA and ALCOA.
83. The Authority notes that determinations made under the Code are not provided in order to assist negotiations made outside the Code. The Authority considers that publishing information in order to assist out-of-Code negotiations would impose unnecessary regulatory costs and be inconsistent with the light-handed negotiate-arbitrate nature of the WA Railway Access Regime.
84. ASCIANO submitted that:
- The Western Australian rail access regime is intended to promote efficient, effective fair and transparent competition on Western Australian rail networks. Pricing certainty and transparency is currently provided by the current maximum and minimum cost submission process.*
- and,
- Any move which reduces the amount of cost information available places access seekers at a disadvantage in price discussions with access providers*
85. The Authority agrees that the current arrangements provide a degree of transparency in relation to railway owners' costs. This does not provide transparency in relation to prices and therefore does not provide certainty in prices, especially where route expansions are required to meet the requirements of access seekers, or there are pre-existing operators using those routes.
86. GIOA submitted that:
- The regular floor and ceiling reviews are an appropriate requirement placed on railway owners who has accepted these obligations as part of the monopoly position their granted ownership places them in, and in the Alliance members' view this is an absolute and minimum requirement for transparency and fairness in this situation.*
87. The Authority agrees that transparency in costs contributes to the achievement of the goals of the WA rail access regime. Nonetheless, it is inaccurate to assert that railway owners have agreed to regular floor and ceiling cost reviews. The Code under which railway owners have agreed to operate, in their lease agreement with the Government (in WNR's case) or their State Agreement Act (in TPI's case) requires floor and ceiling cost reviews as outlined in clauses 9, 10 and 12.
88. GIOA submitted:
- The mid-west iron ore industry shall have a very significant rail freight transport task which is at the core of the developing projects' capital and operational cost structures. The ERA approved floor and ceiling costs are not only critical to negotiations between access seekers and railway owners, they are an essential reference for all stages of project development from pre-feasibility, bankable feasibility to financial close.*
- and,
- ERA determined floor and ceiling costs for rail access are critical for modelling mining and above-rail feasibility scenarios both within and potentially between networks*

without the onerous need on both parties to seek such information under an access application.

and,

The availability of ERA pre-determined floor and ceiling costs enable a potential access seeker to have confidence in their dealings with the Railway Owners and that their proposals for rail access are formed on a reasonable basis.

89. The Authority agrees with the sentiment expressed in these points of view, and agrees that transparency of costs coincides with the intent of the WA Rail Access Regime. The Authority notes that the use of the word 'proposal' in the context of an access proposal as defined in section 8 of Part 2 of the Code does not include a proposal for price.
90. GIOA submitted:
- Irregardless of whether a section of line has a floor and ceiling price determination under the arbitrate and negotiate regime model, if an access application is received under the Code, both the railway owner and the authority [sic] would have to address the specific application. Alternatively, if negotiations are conducted outside the code [sic] the floor and ceiling prices of similar lines are a negotiation guide for the access seeker, as is the case with grain lines.*
91. The Authority notes that the lodgement of an access proposal by an access seeker requires a determination of costs for the relevant route section(s) by the Regulator. This determination may coincide with a pre-existing determination. Cost determinations mandated by the Code are required in order to administer railway owners' Over-payment Rules, and are not published as a negotiation guide for prices agreed outside the Code.
92. GIOA submitted:
- Published floor and ceiling prices together with the regulated component costs and the Costing Principles under the Code are a fair basis for determining the cost of expansion applications where the railway owner and access seeker may disagree on the extent and cost of the expansion.*
93. The Authority notes that capital expansions required to meet an access proposal are likely to be very site and operator specific, and the cost of those expansions are unlikely to be indicated by the costs associated with the unaugmented route section. The Code provides for the Authority to review the replacement cost of an expanded route section when the expansion works have been completed (clause 12). The Authority agrees that publication of railway owners' costing principles provides a useful level of transparency in relation to the costing method that will be used by the railway owner.
94. NWI submitted that the availability of transparent floor and ceiling costs for rail access and public knowledge of both the level of floor and ceiling costs and the basis on which they are formed are critical to the effectiveness of the WA Rail Access Regime.
95. The Authority agrees with this statement. In particular, the Authority endorses the view that transparency should apply to the basis for cost calculations (i.e. asset populations) and the method of cost calculations (the costing principles).
96. NWI submitted:

When a new section of line is established, the railway owner should develop new floor and ceiling prices applicable to the new "Section of Line" for endorsement by the Authority.

97. The Authority agrees that where new sections of line are constructed, and where the new sections of line are included in Schedule 1 of the Code, that the provisions of the Code should be applied to that new section in the same way as they are applied to the existing network. The Authority notes that the existing provisions of the Code do not require the Regulator to make determinations on floor and ceiling prices.

98. NWI submitted:

It is of critical importance to proponents that for planning and capacity calculation purposes that the railway owners [sic] floor and ceiling costs are provided as well as complete and clear information regarding their calculation.

and,

Independently determined floor and ceiling costs are critical for modelling below-rail and above-rail feasibility scenarios both within and potentially between sections of line without the onerous need on both parties to seek such information under an access application.

and,

Such feasibility monitoring is done on an ongoing basis by many potential users and above rail operators.

99. The Authority acknowledges that transparency of costs is critical to business development and planning by upstream producers who require access to railway infrastructure. The Authority understands that the critical element for adequate transparency of costs is the technical description of the asset (i.e. the basis for the cost calculations) rather than the cost calculation itself. The railway owners' costing principles, which are required to be provided to an access seeker following the lodgement of an access proposal, under section 9 (Part 2) of the Code provide the foundation for transparency in cost calculations.

100. The specification of the railway including asset populations (i.e. the number and spacing of sleepers, ballast formation profiles, rail specific weight and tonnage etc) is required in addition to the costing principles to allow a potential access seeker to estimate costs. The per unit costs of asset components fluctuate over time. If an access seeker is able to see an accurate asset population schedule and is able to test the per unit market price of each element of the asset population, a robust estimate of railway replacement cost for planning purposes may be calculated.

101. In WNR's case, the WNR costing model (referred to by WNR as the 'Asset Pricing Model') published as part of the most recent determination of costs by the Authority, provides the requisite asset population data, and a reliable estimate of replacement costs may be calculated by an entity with adequate resources to discover the current per unit market costs of those assets.

102. WNR submitted:

provision for the update of floor and ceiling costs (and therefore access prices) due to indexation and changes in WACC should be considered in the Code – either as something to be stipulated in the Costing Principles, or perhaps more appropriately, one of the matters for which provision is to be made in an access agreement.

103. The Authority notes a number of suggestions for amendments to the Code to improve the adequacy of timeframes specified for processes governed by clauses 8 and 9, and will consider some matters raised in submissions in conjunction with the current review of the Code where resolution of those matters might require amendments to the Code.
104. The Authority notes that requirements for annual adjustments to floor and ceiling costs are not mandated in the Code, but in the Authority's determinations. The current practice of the Authority is to make determinations which are current for three years, and which incorporate two years subsequent adjustments for CPI and WACC as a component of the determination.
105. The Authority further notes that the Code does not require that access prices on a route are directly determined by floor and ceiling costs, as implied in WNR's argument, but that floor and ceiling costs provide lower and upper bounds for revenue recovery on a route.
106. The Authority also notes, in relation to WNR's suggestion that Schedule 3 of the Code be amended such that access agreements make provision for access prices to be linked to indexation of costs, that there is nothing in Schedule 3 that prevents this from being agreed between the railway owner and the access seeker in an agreement.
107. The Authority does note, however, that for the purposes of the Over-payment Rules, the most recent relevant determination of ceiling costs applies. The ceiling cost of a route section may increase independently of the requirements of any of the existing operators on a route if, for example, an additional operator is given access to the route inside or outside the Code.
108. The Authority considers that the railway owner is able to appeal for a redetermination of costs under clause 12 on the basis of a material change in circumstances, which would include a change in per unit asset prices.
109. Clauses 9 and 10 require that costs be determined in respect of nominated route sections. These clauses do not stipulate a maximum or minimum period over which the determination applies.

Additional Matters raised by the Authority

Provision and publication of costing models

110. There is no requirement in the Code for railway owners to provide costing models for publication. Nonetheless, a costing model, incorporating schedules of asset populations, unit costs and a summation of cost components, is an integral part of any initial determination of floor and ceiling costs by the railway owner.
111. The Authority considers that a costing model is an essential part of a railway owner's initial determination, due to the empirical nature of the determination. If an initial determination did not contain a costing model, then the determination would not be able to be reviewed with any clarity. The Authority therefore takes the view that, if it chooses to publish the initial determination as a part of a consultation process, it should publish a railway owner's costing model as a part of that initial determination.

112. There are provisions in WNR's and TPI's Costing Principles which provide for the publication of a non-confidential version of their costing models alongside their initial determinations of floor and ceiling costs.
113. The Authority is confident that stakeholders and their consultants are well-equipped to make adjustments to these costing models for the purposes of updates due to changes in prices, including the cost of capital, or as a basis for extension or expansion planning.

Determination of Costs where a route expansion or extension is required

114. The Authority notes that under section 8(4) of Part 2 of the Code, an access proposal may be made under clause 10 which specifies an extension or expansion that would be necessary to accommodate the proposed rail operation.
115. Section 9(2) of the Code applies if a railway owner receives such a proposal. The floor and ceiling costs and prices required to be provided to the access seeker within 7 days need apply only to the route and infrastructure as it exists and not for access to any proposed extension or expansion. Section 9(2) also requires that the railway owner must, within 30 days of receiving the proposal, provide the proponent with a reasonable preliminary estimate of the costs relating to the proposed expansion and the share of those costs that is likely to be borne by the proponent.
116. The Code does not contemplate a determination being made by the Authority in respect of the estimated extension or expansion costs associated with an access proposal, only that a determination be made in respect of the floor and ceiling costs applying to the route as it exists.
117. The estimate of extension or expansion cost required to be provided under section 9(2)(b)(i) of the Code together with the replacement cost for the unaugmented route section does not constitute a capital replacement cost as defined in Schedule 4 for the augmented route. It would not be appropriate to review floor and ceiling costs for an augmented route determined on the basis of the sum of these two amounts.
118. The Authority notes that, if an access proposal requiring a network extension or expansion proceeds to an agreement under the Code, a determination of costs associated with the augmented network would be needed for the purposes of administering the Over-payment Rules in respect of the route section(s) subject to the agreement.
119. The Authority considers that it is in the railway owner's interests to have floor and ceiling costs for an augmented route section determined as soon as possible after it is built. If a cost determination is not approved prior to operations under a Code agreement commencing, then the railway owner may be unable to recover adequate costs without breaching section 47(2) of the Code, which prescribes compliance with railway owners' Over-payment Rules.
120. The Authority also notes that negotiations for access requiring extension or expansion typically require between 18 months to three years to finalise, and that this provides an adequate lead-in time to facilitate a timely redetermination of costs.
121. A determination of costs for the augmented route section would be undertaken by the Authority under clause 12, that is, due to a change in the specification of a route section for which a determination under clause 9 or 10 has previously been made.

122. An access seeker will be able to obtain advice as to the reasonableness of the estimate for route extension or expansion, and can make a decision as to whether or not they will enter into an agreement with a railway owner on that basis.
123. A determination by the Authority of costs applying to an augmented route will not impact on any price previously negotiated between the railway owner and the operator, nor on any other elements of an agreement negotiated under the Code. A ceiling cost will impact only on the total amount recoverable from that route by the railway owner, and will not prejudice any further redetermination of costs which may be required if, for example, an additional access proposal requiring further expansion be made on that route by another access seeker.

Final Decisions of the Authority

The Authority will require railway owners to submit floor and ceiling costs for their network on commencement of the application of the WA Rail Access Regime to their network.

124. This mirrors current Authority practice.
125. This requirement will be on the basis that it is a reasonable expectation that the application of the regime to the network implies a likelihood that an access proposal may be received. This determination will therefore be required under clause 9 of the Code.

Consultation under clause 9 (Schedule 4) for determinations in respect of route sections for which costs have not previously been determined will incorporate the publication of the railway owner's initial determination and the Authority's final determination on the Authority's website.

126. This mirrors current Authority practice.
127. The Authority will publish the railway owner's initial determination including a costing model, will seek public consultation on those documents and publish the final determination by the Authority.
128. The costing model associated with the railway owner's initial determination will provide sufficient asset population data for access seekers to make their own assessment of costs over subsequent periods, if required, taking into account the applicable Weighted Average Cost of Capital and any changes in asset unit prices over time.

If an access proposal is received, the railway owner must notify the Authority and must submit an initial determination of costs as required under clause 10 (Schedule 4) of the Code.

129. If the railway owner submits an initial determination which coincides with a current (previous) determination by the Authority, then in the absence of any mitigating circumstances, the Authority will approve the railway owner's initial determination. This mirrors current Authority practice.
130. In the case of a clause 10 determination, the Authority will not seek public consultation without the agreement of the access seeker for an adequate extension of the 30 day time limit specified in clause 10.

131. The Authority will not publish the railway owner's initial determination or the Authority's final determination under clause 10 unless the access proposal proceeds to an agreement under the Code. This in no way limits the railway owner's responsibility to provide any of the information which has been provided to a proponent, as described in section 9(1)(c) of the Code to any other entity on request.

Costs for route sections previously determined under clause 9 or 10 (Schedule 4) may be redetermined by the Authority under clause 9 if the Authority expects it likely that a new access proposal will be made.

132. The Authority would, in practice, only form such an expectation in response to an approach by a railway owner or an access seeker detailing a prospective access proposal. Consultation required under clause 9 for determinations in respect of route sections for which costs are being determined for the first time will not incorporate the railway owner's initial determination or the Authority's final determination unless an access proposal is made which proceeds to an agreement under the Code.

All floor and ceiling costs which are published in relation to clause 9 or 10 (Schedule 4) determinations which proceed to an agreement under the Code will apply for five years and will incorporate four subsequent annual adjustments to ceiling costs for changes in CPI and the WACC published annually by the Authority.

133. The purpose of the annual cost adjustments is to enable the administration of the railway owner's Over-payment Rules in relation to revenues received under Code agreements and to enable ceiling costs to reflect a reasonable return to the railway owner over the five year period without requiring the railway owner or the Regulator to redetermine costs over that period.

134. Ceiling costs determined for the purposes of administering a railway owner's Over-payment Rules will remain unadjusted following the expiration of the five year determination period, unless superceded by ceiling costs approved by the Authority in a subsequent determination.

135. Current Authority practice is for determinations to apply for three years, and to incorporate two annual adjustments.

Costs for route sections previously subject to a determination under clause 9 or 10 (Schedule 4) may be redetermined by the Authority under clause 12 (Schedule 4) in response to a request in writing from the railway owner.

136. This will be relevant where a five year determination period has expired and there has been no change to the physical specification of the route section, or other changes except the replacement value of the asset (as defined in Schedule 4). In such instances, and as part of a consultation process contemplated in clause 12(3)(b), the Authority will require the railway owner to make a submission by way of an initial cost determination to facilitate the railway owner's request for a redetermination.

137. This is the mechanism that will be used by the Authority to enable a railway owner to initiate a redetermination of costs, if a railway owners wishes costs on a route or route section to be redetermined. A railway owner may seek to have the costs for a route redetermined, if the route is subject to an agreement under the Code from which revenues are increasing over time. Under these circumstances, revenues

may breach the 'ceiling price test' described in clause 8, if the ceiling cost is not redetermined.